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THE BUSINESS MAN'S VIEW OF CURRENCY REFORM¹

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AS Chairman of the Currency Committee of The Merchants' Association of New York, I am invited to discuss the question of currency reform from the point of view of a business man. I shall waste no time in pointing out the defects of bond-secured bank notes or the need for an elastic currency. On these points all competent students are in agreement. They are agreed as to the evils of the present system and the principles upon which reform should be based. There are but two things which it is necessary to consider: the method of applying the reform principles upon which all agree, and that of creating among the general public a knowledge both of the principles and of their proposed application.

The methods of currency reform that are worthy of serious discussion divide themselves into two classes: Those providing a central control, and those permitting the banks of the country to issue bank notes under certain rules up to an established limit, without central control. While the committee for whom I speak recognize the force of the arguments which have been advanced against central control, our conclusion is that it is the best method to adopt. In speaking recently upon this subject, I stated that we had eliminated as unimportant all objections to central control except four. These are as follows:

First, a fear on the part of many that the control of our currency will pass into the hands of politicians.

Second, the danger of control by special interests.

Third, the fear of exclusive control by the banks of the country.

¹ A paper presented at the meeting of the Academy of Political Science, November 11, 1910.

Fourth, the feeling on the part of some bankers that any currency control which takes the form of a central bank will prove to be a competitor in their business.

These four objections I believe exist, and must be recognized. I am sure, however, that the final analysis will show that only one of them is really to be feared; that is, control by special interests. If the general public can be satisfied that any system of control adopted can be administered for the good of the country and that all selfish interest can be absolutely eliminated, the objections to a central bank will end.

The proposition for which we stand is to design a method of selecting a board of governors of a central bank of certain limited functions, so that selfish interest can never dominate its administration. The opponent of this proposition usually dismisses the whole matter with the sweeping statement that this cannot be accomplished. We do not believe this to be true. Other nations have succeeded in controlling their currency through the medium of a central bank without finding this danger insurmountable, and we believe that if the object to be attained is recognized at the outset, and every safeguard provided, the people of this country are quite as capable of creating a currency control free from the influence of selfish interests as are our commercial competitors abroad.

Modern government and world progress rest upon the exercise of human judgment. If we admit that it is impossible to select administrative agents to whom under established restrictions we may delegate certain powers, government by the people must fail. We have seen many instances of the misuse of powers so delegated, but this has been the case only where the powers granted have been dangerously general in character, or where the people have been so busy with their everyday vocations that they neglected proper supervision of the officials selected.

Public sentiment when aroused is nearly always correct. In its resentment it frequently goes to extremes, but at the base of all great movements of the general mind of the country is to be found a desire for justice. In deciding whether we shall establish well-defined restrictions for the control of our currency and

then delegate its administration to a central board, or whether we shall attempt to create for all time a method which can be successfully operated without such control, we must recognize the dangers of both plans.

We have seen many cases where the power of control was selfishly used, but we have also had frequent experience of the danger of banking methods that lack such control. If in recent years there had been a central board supervising our banking and currency, equal in dignity and importance to the Supreme Court of the United States, a number of gentlemen who are now living at public expense might be successfully conducting their banks. This danger is quite as real as the danger of misuse of the powers which we delegate. It is true that the comptroller of the currency has the theoretical power to prevent unsound banking, but it is most difficult for him to detect improper methods in time.

If, however, the method of note issue were through a rediscounting of commercial paper by a central bank, a direct check upon unsound operations would be created, which could not fail of successful operation. The moment a bank improperly operated was refused the privilege of rediscount its position and usefulness in its community would be ended. In determining, therefore, the relative dangers of a controlled or an uncontrolled currency system, the importance of these considerations must be weighed.

The natural optimism of the people of the United States, perhaps our greatest asset, is another reason why we should delegate to some of our best minds power to check expansion, when it has gone far enough. If we create an automatic system which will permit each bank to issue currency up to say one hundred per cent of its capital stock, there are many who will consider this as a recognized part of their assets, and will expand their operations as recklessly to this limit as to those which are at present provided, and we shall find that no safety check has been created.

We are against an uncontrolled system also for the reason that such methods are as yet untried by any great nation. The only example of any importance of such a system is that of

Canada to-day. Canada has a population of about seven million. Its problems of international finance are nothing as compared with those of this country, and in times of financial stress it has both England and the United States to fall back upon.

We object to an uncontrolled system again, because it provides no medium for the protection of our gold reserve through dealings in gold and foreign exchange. The power to safeguard this point is absolutely essential, and it requires, in an emergency, the exercise of our best banking and business judgment.

We are against an uncontrolled system because we recognize that if rules to govern our financial operations had been adopted fifty years ago, based upon conditions as they then existed, they would be outgrown and hopelessly inadequate to-day, and we do not believe that it is possible for the present generation to provide regulations which will meet the unknown developments of the future.

Most systems of currency issue which do not provide for central control are based upon what is known as asset currency. These schemes vary in detail, but the general plan is to issue currency against the assets of the bank. As business men we are against asset currency because we believe it is a first cousin to bond-secured currency which makes it mandatory that bank notes be issued against an investment in fixed securities. Asset currency makes it permissive that this be done. We believe that the funds of the depositor, which are a demand obligation, should not be invested in fixed securities, but should be held as nearly liquid as possible, to meet the requirements of trade. The banking experience of the world has shown that this object is best attained by the investment of these funds in short-term commercial paper, which can be readily liquidated within a limited number of days. Asset currency in its usual form makes it possible for a bank to invest its assets in bonds or underwritings, and to issue bank notes against them.

We also believe that it is impossible to create an uncontrolled system which will permit the centralization and proper administration of our reserves. This is a most important point. If our reserve is scattered among 20,000 banks, it may be as great

in the aggregate, but it cannot be so effective in preserving public confidence, as if centralized in one great reservoir where we all may see and measure its immensity. It is, of course, quite possible to design an uncontrolled system, which will state that the reserves must be held in one central reservoir, but the moment you attempt to administer this reserve properly the power of control must be delegated to someone. I have listened to addresses in which an apparently automatic system was carefully worked out, until the point of administering the reserves was reached. Then the author, who has usually devoted the first half of his speech to denouncing methods of central control, has calmly turned over to certain government officials, or others, the administration of this enormous mass of money, upon which our whole currency and banking system finally rests. This brings me to the point that nearly every recent plan for the reform of our currency either openly provides some board of central control, as in the general clearing-house plan or else covertly recognizes its necessity by delegating to someone the power to administer reserves. If this is so, are we not really quarreling over the selection of a name?

There are to be found in various parts of the country many who believe that we cannot delegate power to a central bank, but are quite certain that the general clearing-house proposition is sound. Where is the real difference? The country is so large that any system must be operated through the medium of branches. Each calls for a board of central control which is as much subject to the danger of selfish interest in one case as the other, and the function of note issue is practically identical. In time of need, the banker takes a portion of his acceptable assets to the nearest operating branch, and receives in exchange an agreed percentage of their value in bank notes and certificates. There may be some trifling difference in detail, but the principle is identical.

The general clearing-house plan does not provide the necessary power and machinery to deal in gold and foreign exchange. Otherwise it is a central bank, except in name. The name we consider important only in its international relation. We have a reputation abroad for trying various kinds of freak

currency. Other things being equal, we believe that it is desirable to adopt the same general methods that are used and understood by other great nations. By doing this we are the gainers.

The central bank which we propose has nothing in common with the two central banks which formerly existed in this country, and is a very limited and restricted form of the central bank employed by other nations. We have now 20,000 banks which are in intimate daily touch with every merchant in each small community. We should do nothing to interfere with the operation of these banks, and we do not propose creating an institution which will in any way compete with them. We suggest delegating two powers only: first, the right to issue notes under certain well-defined conditions, in exchange for approved short-term commercial paper; and second, the power to deal in gold and foreign exchange. We do not even insist that a central bank be made the financial agent of the government. In our opinion this will be desirable, but it is not an essential part of our currency system, and it is our aim to reform that system first, without introducing unnecessary details and complications.

I now come to my second point, which is, how to create a more general knowledge of this most important subject. As I look back upon the speeches which I have made, and remember the addresses to which I have listened, it seems to me that all of us, when discussing this subject before a lay audience, make a profound impression upon ourselves, but leave those who have been patient enough to listen, with the idea that the subject is intensely complex and far beyond their understanding. This is unfortunate, because in reality the underlying principles are simple and readily understood.

The present situation is complicated, of course, by the fact that we have seven hundred millions in bank notes secured by government bonds, which the government has forced the bankers to purchase at a rate of interest not warranted by investment conditions. Before a banker purchases bonds as a basis for circulation, he estimates the value of the money which he is investing. The notes which he is enabled to issue must find employment, and unless the operation is profitable it is not under-

taken. This means that the general public in the end pay a proper rate of interest upon the bonds of the government, through an increase in the cost of their currency. If this simple fact is made clear, popular sentiment will be in favor of refunding our government bonds at a rate of interest which will cause them to be sought as an investment.

A number of ingenious methods have been suggested by which we take money out of one pocket and put it into another, to pay off these bonds. By far the best method is to meet the issue fairly and squarely, to borrow in the investment markets of the world what money the government may need, paying a fair rate of interest and not complicating our currency situation.

Once we have overcome this difficulty, we are able to make a fresh start, and it is of the first importance that students of this question, such as are gathered here to-day, and those who speak upon the subject, endeavor to impress upon the general public the simplicity of the problem, and to make them realize how readily it can be understood by the lay mind. Point out to them, for instance, that the functions of any note-issuing institution are merely those of a bank for banks. The man who is operating even the simplest industry will understand this, if you compare the bank's situation with his own. When conditions arise which make it impossible for him to collect as readily as usual the accounts due, or when through some change in trade conditions he finds himself with a larger amount of merchandise in stock than he can comfortably carry, he goes to his banker and explains his condition. If it is sound he pledges certain of his assets or his commercial paper properly endorsed, and obtains assistance until normal conditions reassert themselves.

When the banking community as a whole has extended all the relief within its power and then finds that collections are slow, or that merchants are overstocked with the merchandise in which they deal, there is no bank to which the bank can appeal for temporary assistance. If a central institution, created for the general good of the entire country, were in existence, the banks in turn would pledge the commercial paper which they hold, and obtain currency to meet the needs of the busi-

ness communities which they serve. There is absolutely no difference in principle, and if the problem be brought down to this level, it will be understood by anyone.

One of the conditions most essential to the successful operation either of the commercial bank which is to help the merchant directly, or of the central bank which helps the merchant indirectly by helping the commercial bank, is that power be intelligently exercised by somebody to say when expansion shall be checked. Many business men know that they have been tided over critical times by their banker, with the understanding that the assistance is temporary and that they must curtail their operations to an amount in proper proportion to their capital. The merchant is saved and is granted time to reconstruct his business upon safe lines. Without this advice and assistance he would have been forced to the wall.

In the same way a bank which has been attempting to carry an amount of business out of proportion to its available capital, may tide over an emergency, but conditions may be insisted on which will avoid the recurrence of the situation. If you will consider the problem from this standpoint, many illustrations will occur to you, and I believe that the greatest good can be done if we start out to correct the impression that the problem is complicated and beyond the understanding of the average individual, and if we undertake to bring this discussion down to the level of understanding of those who conduct the most simple industries of the country.